

## ECONOMIC AND SOCIAL REFORMS IN UKRAINE: CHALLENGERS FOR GOVERNANCE

## ЕКОНОМІЧНІ ТА СОЦІАЛЬНІ РЕФОРМИ В УКРАЇНІ: ВИКЛИКИ ДЛЯ АДМІНІСТРУВАННЯ

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*The article deals with the problem of governance and its dynamics due to realization of reforming Ukrainian business sector. The purpose of the article is to determine the impact of the domestic economy reforming on the indicators of the country's governance. To achieve this purpose such stages were performed: analysis of the main results of the reforms of the national economy; assessment of the dynamics of the level of competitiveness and the level of globalization of the country; assessing the dynamics of indexes of governance for transitive economies developed by international institutions. The dynamics of world governance indexes and transition indexes for Ukraine were analysed. On the basis of such analysis the SWOT analysis matrix for the level of governance and investment climate of Ukraine was built. The level of Ukrainian transition and governance indexes prove, that country have to do a lot to correspond to the standards of a sustainable market economy.*

**Key words:** *Ukrainian reform process, globalization, Foreign direct investments, transition economics, World bank governance indexes, SWOT-analysis*

*Стаття посвячена проблемі адміністрування в сучасних умовах реформи*

*рвання економіки України. Цель статьи – определить влияние реформирования отечественной экономики на показатели администрирования страны. Для достижения этой цели были выполнены такие задания: проанализированы основные результаты реформирования бизнес-сектора; дана оценка динамики уровня конкурентоспособности и уровня глобализации страны; дана оценка динамики показателей администрирования, специально разработанных международными институтами для переходных экономик. Проанализирована динамика показателей администрирования и переходных показателей для Украины. На основе такого анализа была построена матрица SWOT-анализа для уровня управления и инвестиционного климата Украины. Уровень украинских показателей переходного периода и администрирования доказывает, что стране нужно многое сделать, чтобы соответствовать стандартам устойчивой рыночной экономики.*

**Ключевые слова:** *процесс реформ в Украине, глобализация, прямые иностранные инвестиции, экономика переходного периода, индексы администрирования Всемирного банка, SWOT-анализ.*

*Статтю присвячено проблемам адміністрування в Україні на тлі проведення економічних реформ. Вона має на меті визначення впливу реформування вітчизняної економіки на показники адміністрування держави. Для досягнення цієї мети вирішено такі завдання: проаналізовано основні результати реформ національної економіки; проведено оцінку динаміки рівня конкурентоспроможності та рівня глобалізації країни; проведено оцінку динаміки індексів адміністрування для перехідних економік, що розроблені міжнародними інституціями; побудовано матрицю SWOT-аналізу для рівня адміністрування та інвестиційного клімату України. Для цього використовувалися дані таких міжнародних інституцій, як Світовий банк та Європейський банк реконструкції та розвитку. Проаналізовано хід проведення реформ в Україні протягом 2014–2018 рр., проведено аналіз динаміки рівня глобалізації та рівня конкурентоспроможності країни. У 2015–2018 рр. уряд здійснив значну кількість реформ, які повинні допомогти Україні реалізувати свій значний інвестиційний потенціал. Проаналізовано динаміку індексів адміністрування та показників, спеціально розроблених для перехідних економік. Аналізуючи дані показників адміністрування, показано, що Україна досягла прогресу в ефективності уряду та контролю над корупцією, однак рівень політичної стабільності значно зменшився за період 2010–2018 рр. Порівняння з відповідними показниками Польщі, Словаччини та Чехії показало, що український рівень адміністрування значно поступається європейським країнам. Рівень українських індексів адміністрування доводить, що країна повинна ще багато зробити для того, щоб відповідати стандартам стійкої ринкової економіки. На основі проведеного аналізу побудовано матрицю SWOT-аналізу для рівня адміністрування та інвестиційного клімату України, де виділено сильні та слабкі позиції, можливості для подальшого розвитку та загрози. Також запропоновано теоретико-методологічні підходи та практичні рекомендації щодо вдосконалення адміністрування та підвищення інвестиційної привабливості країни.*

**Ключові слова:** *процес реформ в Україні, глобалізація, прямі іноземні інвестиції, економіка перехідного періоду, індекси адміністрування Світового банку, SWOT-аналіз.*

**Formulation of the problem.** Ukraine has been subject to a number of attempts of economic reform since independence, but has not managed to fully transition to a market-based system. Previous efforts have failed to combat inconsistent macroeconomic policies, unsustainable energy pricing, and corruption. As a result, the Ukrainian economy has ended up in a semi-transformed state with many shortcomings.

**Actual scientific researches and issues analysis.** The effectiveness of Ukrainian reforming process has become a central element of many studies of scientists and institutions. They investigated the impact of reforms on investment climat of the country/ level of risks, attractiveness of Ukraine for foreign investors.

American Chamber of Commerce (ACC) each year prepare a profile of Ukraine (the same as profiles of another countries). In profile for 2018 it was noticed, that the main factors for foreign investors to increase a volume of investments in the defined country are a favorable business environment, macroeconomic and political stability. To the main challenges of Ukrainian business sector experts include: corruption, imperfection of the legislative framework, political instability [1].

European Commission in Association Implementation Report on Ukraine pointed out that "...Ukraine has the potential to attract more foreign investments. International rankings point to legal and judicial unre-

dictability and an inadequate institutional framework as the main obstacles to improving the business and investment climate...” [5].

The World Bank identifies four “pathways”, or areas, along which Ukraine needs to develop and reform in order to achieve a sustainable recovery. The most important, is building institutions of better governance and anti-corruption. For this Ukraine needs to prioritise the reforms of public fiscal management, anti-corruption and justice institutions, the public administration reform, and citizens’ engagement [12].

Balázs Jarábik, Thomas de Waalt pointed out, that the biggest constraint on growth in Ukraine is low investment. Gross capital investment amounts to 15 percent of GDP, well short of the 25 percent necessary for Ukraine to reach annual growth rates of 6 or 7 percent. Investors’ confidence has grown slightly according to a survey by the European Business Association, but corruption, weak rule of law, and the war in the east remain formidable deterrents [8].

At [2] authors give a detailed analysis of a composition of the foreign investment and investment behaviour in the economy of Ukraine within 2011-2015 years. The main reasons of decrease in the volumes of investment into economy of Ukraine are determined such as the political and economic situation slows the growth of investment not only in the country but also abroad.

S. Oxenstierna, J. Hedenskog described a process of Ukrainian reforms and focused on low level of governance [7].

A. Wilson concentrated on reaction of foreign business entities on Ukrainian crisis and opportunities of international agencies to assist in overcoming it [10].

A lot of authors also pointed out the imperfect governance at national business sector [1; 2; 5; 7; 8; 12]. Governance consists of the traditions and institutions by which authority in a country is exercised. This includes the process by which governments are selected, monitored and replaced; the capacity of the government to effectively formulate and implement sound policies; and the respect of citizens and the state for the institutions that govern economic and social interactions among them [6].

Although there are a lot of investigation about results of Ukrainian reforms, due to the strengthening of the political and economic crisis, the continuation of hostilities in the East, and the abrupt contraction in foreign investment, caused by these phenomena, the feasibility of further scientific development of the problem of governance remains unchanged. This state of the problem determines the need to analyze the challenges of governance of Ukrainian economy at the present stage and to develop an effective and adaptive mechanism of its improvement.

**The purpose of the article** is to determine the impact of the domestic economy reforming on the

indicators of the country's governance. To achieve this purpose we have to provide such stages: analysis of the main results of the reforms of the national economy; assessment of the dynamics of the level of competitiveness and the level of globalization of the country; assessing the dynamics of indexes of governance for transitive economies developed by international institutions; construction of a SWOT analysis matrix for the level of governance and investment climate of Ukraine.

**Methods used.** To achieve a purpose of investigation such general scientific and special methods and techniques were used: theoretical analysis and synthesis, methods of grouping, modeling, comparison, economic-statistical, graphical representation, as well as methods of systematization and scientific generalization.

**Main results.** Ukraine has been subject to a number of attempts of economic reform since independence, but has not managed to fully transition to a market-based system. The International Monetary Fund (IMF) and other international donors have been engaged in this work since the 1990s, but previous efforts have failed to combat inconsistent macroeconomic policies, unsustainable energy pricing, and corruption. As a result, the Ukrainian economy has ended up in a semi-transformed state with many shortcomings.

During 2015-2018, the government has taken a significant number of reforms which should help Ukraine to realize its large investment potential. In fact, more economic reforms has been taken in 3 years than during the entire period since independence in 1991 [7] (Table 1).

The reforms undertaken over the last three years are already improving the investment climate in Ukraine. In fact, a comparison in the ranking of Ukraine in the Doing Business Reports of the World Bank and IFC shows that Ukraine has made significant improvements from 112-th position in 2014 to 76 place at 2018.

As about globalization, Ukraine can hope to take its proper place in global integration processes, while at the same time gaining significant advantages, namely: using the latest achievements of scientific and technological progress, participating in the world division of labor on the basis of self-analysis and creating a favorable legal and infrastructural environment; increase of tourist flow; increase in volumes of direct and portfolio foreign investment. If we analyze the dynamics of the globalization index of Ukraine, it is noticeable that de-jure indicators (they analyze the existence of mechanisms and infrastructure of globalization) are greater than de facto ones (they explain the results of acting mechanisms and policies) [9]. The institutional mechanism for promoting globalization is created, but it is not really involved in processes of economic, social and political nature.

Table 1

**Main results of reforms in Ukraine during 2015-2018**

Direction of reforms	Main results
1. Macroeconomic stability	<ul style="list-style-type: none"> <li>The Fiscal budget deficit has been brought under control</li> <li>The Central Bank has followed prudent monetary policies</li> <li>The Central Bank has moved towards a flexible FX rate regime</li> <li>Inflation down to 12.5% at year-end and exchange rate stabilized</li> </ul>
2. Reform of Taxation, Government Expenditures & Customs	<ul style="list-style-type: none"> <li>The number of taxes have been cut from 22 to 11</li> <li>The payroll taxes were cut in half from a high level to 22% of wages</li> <li>A single retail price for natural gas was set close to international prices •As a result, the gas company, Naftogaz, has eliminated income losses</li> <li>New electronic public procurement system has been put in place</li> <li>Procurement of medicine has been outsourced</li> <li>Single portal on public funds use has been created</li> </ul>
3. Eradicate Corruption	<ul style="list-style-type: none"> <li>A Prosecutor General was appointed with the task to reform the system</li> <li>Three anti-corruption bodies have been put in place and are already working</li> <li>A new electronic assets and income declaration for Govt officials is in place</li> <li>Legal procedures has been initiated for 150 officials suspected of corruption</li> </ul>
4. Legal and Judiciary Reform	<ul style="list-style-type: none"> <li>The Constitution was adjusted to permit judiciary reform</li> <li>The Lustration law approved to dismiss corrupt judges and officials</li> <li>A new police has been established</li> </ul>
5. Improve public administration	<ul style="list-style-type: none"> <li>The size of government has been reduced</li> <li>“One-window” form most public administration services has been established</li> <li>Have started fiscal decentralization with local revenues about 20% of the total</li> </ul>
6. Develop the financial sector	<ul style="list-style-type: none"> <li>Banking system more stable thanks to the closure of 80 weak banks</li> <li>Banking supervision improved with stress tests and re-capitalizations.</li> <li>Banks have opened information about their final beneficiaries and owners.</li> </ul>
7. Deregulate business activities	<ul style="list-style-type: none"> <li>A moratorium for business inspections is in place.</li> <li>A number of controlling agencies were eliminated (i.e., veterinary, sanitary)</li> <li>Open state registries and databases</li> <li>Management of state firms improved and cut income losses by 85%</li> </ul>
8. Reform International trade/capital	<ul style="list-style-type: none"> <li>FTA with EU and Canada in place</li> <li>New FTAs with Israel, Turkey</li> <li>Foreign debt was restructured</li> </ul>
9. Reduce Political Risks	<ul style="list-style-type: none"> <li>No conflict between President-PM both with pro-EU orientation (even after President and Parliament Election at 2019 the future prime-ministed will be elected by propresidential coalition at parliament)</li> <li>TV channels/radio list owners.</li> <li>Actively engaged the US/EU to contain Russian aggression</li> <li>Strengthen local military forces</li> </ul>

To assess the progress of Ukraine in achieving better governance, one can use indicators and ratings of different international agencies. In our investigation we use World Governance indicators (WGI), represented by World Bank [11] and transition indexes, calculated by European bank of Reconstruction and Development (EBRD) [3].

World Bank construct two measures of governance corresponding to each of these three areas, resulting in a total of six dimensions of governance, which lies on basis of correspondent World Governance Indicators (WGI) [6]:

– *The process by which governments are selected, monitored, and replaced:*

1. Voice and Accountability (VA) –country's citizens ability to participate in selecting their government, as well as freedom of expression, freedom of association, and a free media.

2. Political Stability and Absence of Violence/Terrorism (PV) –likelihood that the government will be destabilized or overthrown by unconstitutional or vio-

lent means, including politically-motivated violence and terrorism.

– *The capacity of the government to effectively formulate and implement sound policies:*

3. Government Effectiveness (GE) –the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies.

4. Regulatory Quality (RQ) –ability of the government to formulate and implement policies and regulations of private sector development.

– *The respect of citizens and the state for the institutions that govern economic and social interactions among them:*

5. Rule of Law (RL) –agents have confidence in and abide by the rules of society, and in particular the quality of contract enforcement, property rights, the police, and the courts, as well as the likelihood of crime and violence.

6. Control of Corruption (CC) – public power is exercised for private gain, including both petty and grand forms of corruption, as well as “capture” of the state by elites and private interests.

Each of six aggregate WGI measures are constructed by averaging together data from the underlying sources that correspond to the concept of governance being measured. The level of each index is valued from -2,5 (low/weak level of governance) to +2,5 (high/strong level of governance) [6].

Dynamics of WGI for Ukraine at 2010-2017 is shown at table 2.

Analyzing the data of table, it is clear, that Ukraine has achieved a progress at Government Effectiveness and Control of Corruption, but the level of Political Stability significantly reduced. However, the level of all WGI is negative (excluding Voice and Accountability). Dynamics of WGI for Ukraine, Poland, Slovakia and Czech Republic also is represented at figure 1.

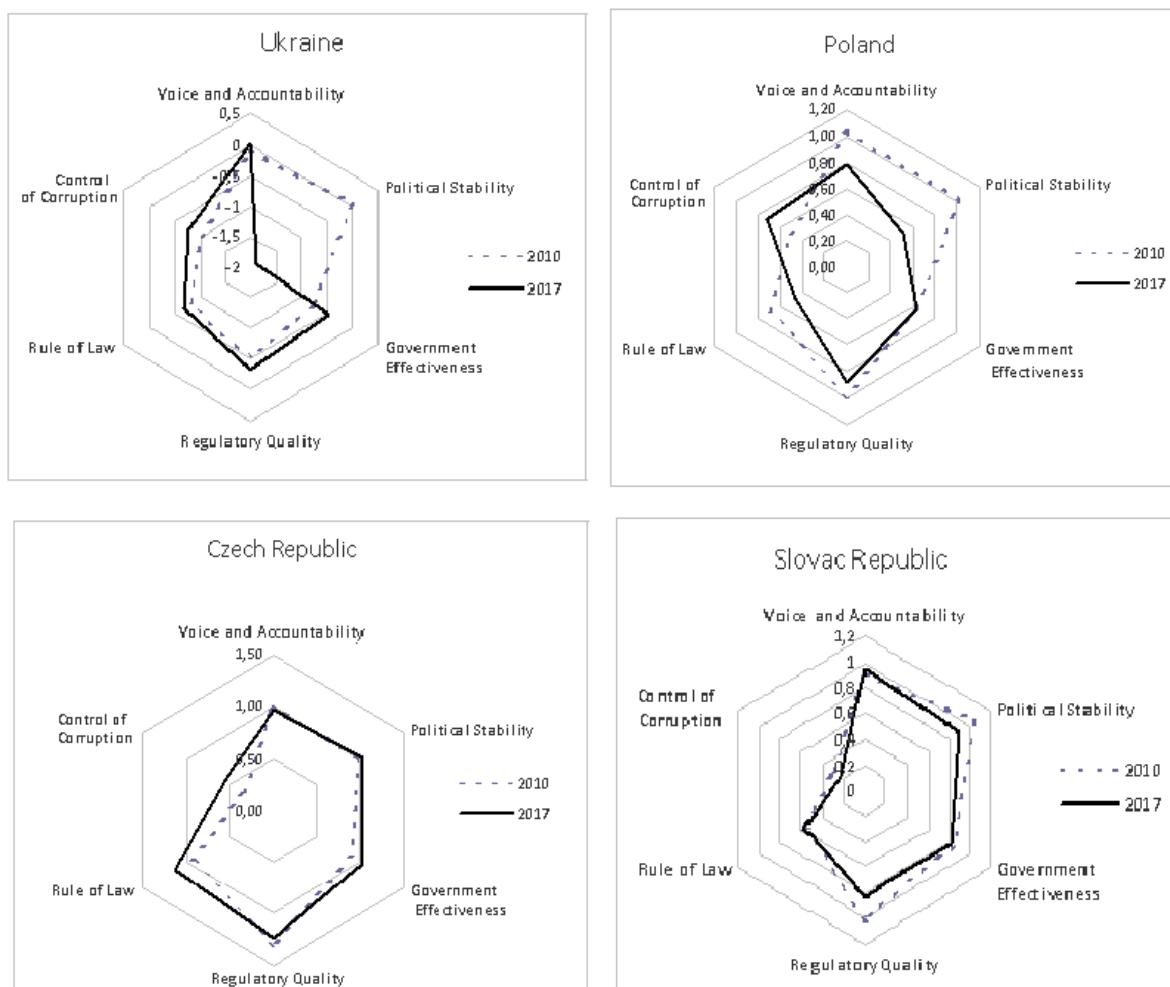


Fig. 1. WGI for Ukraine, Poland, Czech Republic and Slovak Republic (authors calculation on the base of World Bank data)

Source of data: [11]

Table 2

World Governance Indexes for Ukraine at 2010-2017

	2010	2011	2012	2013	2014	2015	2016	2017
Voice and Accountability	-0,08	-0,13	-0,28	-0,32	-0,14	-0,09	0	0,01
Political Stability	0,01	-0,07	-0,09	-0,78	-2,02	-1,96	-1,86	-1,89
Government Effectiveness	-0,78	-0,82	-0,58	-0,65	-0,41	-0,52	-0,57	-0,46
Regulatory Quality	-0,52	-0,6	-0,6	-0,62	-0,63	-0,59	-0,43	-0,32
Rule of Law	-0,81	-0,82	-0,78	-0,8	-0,79	-0,81	-0,77	-0,71
Control of Corruption	-1,03	-1,05	-1,08	-1,13	-0,99	-0,98	-0,81	-0,78

Source of data: [11]

It is worth to notice, that the levels of WGI at all analyzed countries is not correspond with the maximum ranks (that is +2.5). The greatest value is about 1.00, that is not enough for european countries. The great regres belongs to Ukraine on the index of Political Stability, while another indexes slightly increased. Also Poland reduced almost all WGI, where Political Stability suffered the greatest falling. As figures shown, the Control of Corruption is general problem to all analyzed countries.

Since 1994, The European Bank of Reconstruction and Development (EBRD) has presented transition indicators for countries in transition that reflect the judgements of the office of the Chief Economist of EBRD about country-specific progress in transition through a set of transition indicators [4].

Following the revision of the transition concept in 2016, the EBRD has developed a new approach to tracking progress in transition. The new methodology assesses developments along six qualities of a sustainable market economy: competi-

tive, well-governed, green, inclusive, resilient and integrated.

The latest update is from 2018, which gives a picture of Ukraine's transition status after reforms started. Comparisons are made with Poland and Slovakia, since these countries come from the same socialist past and had a similar standard of living in 1991. Table 3 depicts the scores for Poland, Slovakia, and Ukraine in 2018 (for Czech Republic EBRD doesn't calculate transition indexes, because this country doesn't belongs to one's with transition economy since 2014). Scores range from 1 to 10, where 10 represents a synthetic frontier corresponding to the standards of a sustainable market economy.

First, it may be noted that Poland and Slovakia, as other EU countries, scores better in all these indicators, and significantly higher than Ukraine. The level of Ukrainian indexes prove, that country have to do a lot to correspond to the standards of a sustainable market economy. The greatest progress is at section

Table 3

**EBRD Transition Indexes for analyzed countries**

	Competitive		Well-governed		Green		Inclusive		Resilient		Integrated	
	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017
Ukraine	4,7	4,6	4,6	4,4	5,8	5,8	6,0	6,0	5,6	4,9	4,9	4,9
Poland	6,6	6,5	6,9	7,1	6,9	6,9	7,1	7,0	8,0	7,9	6,8	6,8
Slovak Republic	7,0	7,1	6,1	6,1	6,8	6,8	6,7	6,6	7,8	7,8	7,4	7,5

Source: [3]

Table 4

**SWOT matrix of improvement of level of governance and investment climate of Ukraine**

Strengths	Weakness
<ul style="list-style-type: none"> <li>- Highly educated labor force</li> <li>- Low wages of USD 300 per month</li> <li>- Ukraine is located in the geographical center of Europe, and has a large border on the EU, with logistic and transportation advantages</li> <li>- Ukraine's large population and great internal market</li> <li>- It has a reasonable infrastructure with extensive railways and road networks</li> </ul>	<ul style="list-style-type: none"> <li>- Corruption Problems</li> <li>- low-level war: Ukraine is fighting against Russian-backed actors in the east</li> <li>- Problems with Resolving Insolvency</li> <li>- Social Conflicts between different groups</li> <li>- Deficit of Energy Sources</li> <li>- Institutional Weakness</li> <li>- Lack of respect for the rule of law,</li> <li>- Poor infrastructure</li> <li>- Lack of capital</li> <li>- The effects of oligarchic monopolies</li> <li>- An overregulated economy</li> <li>- Domestic political fights due to 2019 president and parliament election process</li> </ul>
Opportunities	Threats
<ul style="list-style-type: none"> <li>- open economy which could grow faster with the new Association and Free Trade Agreements with the EU and Canada, and expected FTAs with Turkey, Israel, and other countries</li> <li>- Ukraine may be used as a bridge in the supply chain from Asia to the EU</li> <li>- Great agricultural potential with high quality fertile land (making it the third world's largest exporter of grains)</li> <li>- Industrial and high-technological potential given past industrial history and high level of university education</li> <li>- Growing interest in the country by multinationals and financial investors</li> </ul>	<ul style="list-style-type: none"> <li>- Military Risks</li> <li>- Economic Stabilization Risks</li> <li>- Political Risks</li> <li>- Foreign Debt Risks</li> <li>- Reputation Risks</li> <li>- Risk of changing of political line-up due to 2019 electoral process</li> <li>- Lack of Stability</li> </ul>

“Inclusive”, but at Ukraine there were not a problem of under-served social groups.

Ukraine during 2018 improved values of groups “Well-governed” and “Resilient”. But a country still have to do much work, especially in macroeconomic and financial stability (a great foreign debt and significant payment to serve it during 2019-2020 years), energy sector diversification. That is why the flows of foreign direct investments (FDI) remain low and opinion about investment in Ukraine as high-risky business has a significant basis.

Ukraine has received a significant volume of foreign direct investments (FDI), but these inflows did not lead to structural changes or technological modernization. In 2017, foreign investors invested \$ 1871.2 million in equity in the Ukrainian economy. From the European Union countries in 2017 Ukraine received \$ 1244 million of foreign direct investment (FDI), and from other countries of the world – \$ 627.2 million.

The inward stock of FDI declined by about USD 15 bn to USD 63.8 bn (48.4% of GDP) over the year. These adverse developments give rise to a number of concerns, as FDI flows serve a dual purpose: they provide stable, long-term capital inflows that can support the external balance of the country, which is still rather shaky, and add to the country's overall investment levels, which are under severe pressure, despite significant reform efforts to improve and deregulate the business and investment climate [12].

On the base of synthesis of existent scientific and research publications, recommendations of international agencies, analysis of the level of governance in Ukraine we propose a matrix of SWOT-analysis of level of governance and investment climate of Ukraine (Table 4).

**Conclusion.** So, the government has taken a significant number of reforms which should help Ukraine to realize its large investment potential and improve an business climate. In fact, more economic reforms has been taken in 3 years than during the entire period since independence in 1991. Ukraine increased its position in Doing Business Reports during 2014-2018 on 38 positions.

However, all efforts did not lead to a significant improvement in the level of governance. The level of Ukrainian transition and governance indexes prove, that country have to do a lot to correspond to the standards of a sustainable market economy.

Today, the main tasks for the state are effective revision of the system of formation and support of FDI in Ukraine, analysis of priorities of the strategy of economic development, determination of the factors causing the ineffectiveness of legislative acts, which are responsible for support attractiveness of the investment climate. In order to achieve this, it is nec-

essary to make a gradual depolitization of the economy, to ensure the consistency of economic reforms, the protection of the market rights and freedoms of the investor.

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## ECONOMIC AND SOCIAL REFORMS IN UKRAINE: CHALLENGERS FOR GOVERNANCE

Ukraine has been subject to a number of attempts of economic reform since independence, but has not managed to fully transition to a market-based system. Previous efforts have failed to combat inconsistent macroeconomic policies, unsustainable energy pricing, and corruption.

**The purpose of the article** is to determine the impact of the domestic economy reforming on the indicators of the country's governance. To achieve this purpose such stages were performed: analysis of the main results of the reforms of the national economy; assessment of the dynamics of the level of competitiveness and the level of globalization of the country; assessing the dynamics of indexes of governance for transitive economies developed by international institutions; construction of a SWOT analysis matrix for the level of governance and investment climate of Ukraine.

**Methods used.** To achieve a purpose of investigation such general scientific and special methods and techniques were used: theoretical analysis and synthesis, methods of grouping, modeling, comparison, economic-statistical, graphical representation, as well as methods of systematization and scientific generalization.

**Main results.** During 2015-2018, the government has taken a significant number of reforms which should help Ukraine to realize its large investment potential.

The dynamics of world governance indexes and transition indexes for Ukraine were analysed. Analyzing the data world governance indicators, it was shown, that Ukraine has achieved a progress at Government Effectiveness and Control of Corruption, but the level of Political Stability significantly reduced. Comparisons with correspondent indexes for Poland, Slovakia and Czech Republic has shown that Ukrainian level of governance significantly inferior european countries. Poland and Slovakia, as other EU countries, scores better than Ukraine in all transition indicators. On the basis of such analysis the SWOT analysis matrix for the level of governance and investment climate of Ukraine was build.

**Practical implications.** The level of Ukrainian transition and governance indexes prove, that country have to do a lot to correspond to the standards of a sustainable market economy. Today, the main tasks for the state are effective revision of the system of formation and support of FDI in Ukraine, analysis of priorities of the strategy of economic development, determination of the factors causing the ineffectiveness of legislative acts, which are responsible for support attractiveness of the investment climate.

**Value/originality.** In our work, we considered an issue of governance at conditions of reforming Ukrainian business sector. The theoretical and methodological approaches and practical recommendations of governance improvement were proposed.